Economic Research

April 2021

Market Monitor – Hong Kong

Labour Market under Pressure

Labour market under pressure

Markit's Hong Kong Purchasing Managers' Index (PMI) rose to 50.2 in February (up from 47.8 in January), reflecting a fractional improvement in Hong Kong's business activities as the Covid-19 outbreak receded and the vaccination programme started that month.

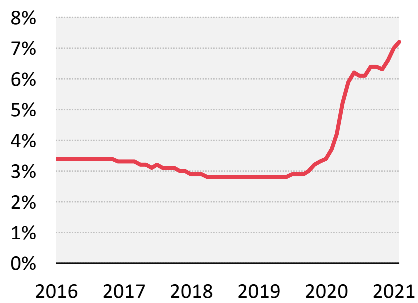
However, the labour market remained lacklustre. The median household income dropped 7.4% annually to an average of HKD 26,600 per month in 2020. The unemployment rate remained elevated, rising to 7.2% in the December–February period, the highest since 2004 and up slightly further from 7% in the November–January period. The unemployment rate in retail, accommodation, and catering services saw some improvement, falling 0.2 percentage points from January to 11.1% after the government loosened social distancing measures in mid-February. However, other sectors saw a deterioration, notably in external trade, the postal and courier sector, and education.

Hong Kong's vaccination programme started on 26th February, and eligibility quickly expanded to cover about 73% of Hong Kong population. By 28th March, about 444,000 people had received their first vaccine dose, accounting for about 5.9% of the population. If vaccination progress continues, social distancing measures can be relaxed. This will be positive for the labour market, especially the retail and catering sectors.

However, a significant recovery is still distant. According to a survey by ManPower Group, over half of employers indicated a freeze in headcount in Q2, while 24% planned to trim their workforce, slightly more than the 22% who planned to increase headcount.

- **Labour market faces challenges of fresh Covid-19 outbreak.**
- **Hong Kong's economy will be boosted by external environment in the short run.**
- **Due to a supply shortage and low interest rates, there will be a modest rise in residential property prices.**

Hong Kong Unemployment rate

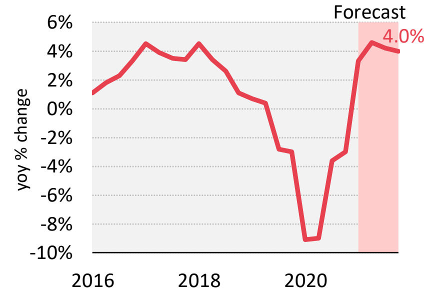


Source: Hong Kong Census and Statistics Department, data as of 17/3/2021

Economic recovery boosted by external environment

In the short run, Hong Kong's economic recovery will depend on the external environment. On the trade front, economic recovery in Mainland China and the US will shore up demand for Hong Kong exports. Improvement in the local market depends on the pandemic situation and domestic vaccination progress this year. Fast progress will shore up investment, consumer sentiment, and economic growth in the second half of the year. On the other hand, the recurrent global epidemic situation and tensions in US-China relations will bring downside risks to the global economy, and hence Hong Kong's economic recovery.

Hong Kong GDP Growth



Sources: Hong Kong Census and Statistics Department; BEA Economic Research Department, data as of 17/3/2021

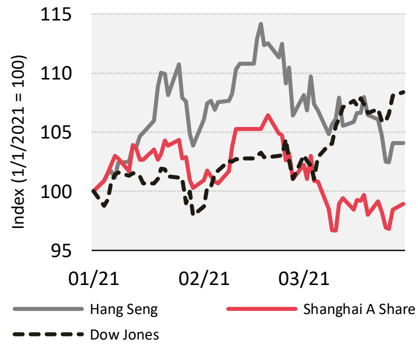
Recent surge in US treasury yields weighs on equity market

The US 10-year Treasury bond yield has risen to a level above 1.7% in March, up from about 0.9% at the beginning of this year. The surge in treasury yields has caused shockwaves in the global stock markets. The rise in yields largely reflected investors' optimism about the US economic recovery. However, this was not good news for technology stocks, whose prices had risen sharply in recent years. Since the valuation of technology companies mainly depends on the company's growth prospects, rather than profit returns, the attractiveness of these stocks decreases against the backdrop of rising interest rates. The Hong Kong Tech Index thus fell 10% between the end of February and 8th March.

Nevertheless, boosted by USD 1.9 trillion in fiscal stimulus, and better-than-expected nonfarm payroll figures in the US, market hopes for a faster global recovery were boosted and investor sentiment strengthened. Stock prices in Hong Kong have been stabilising from their recent lows.

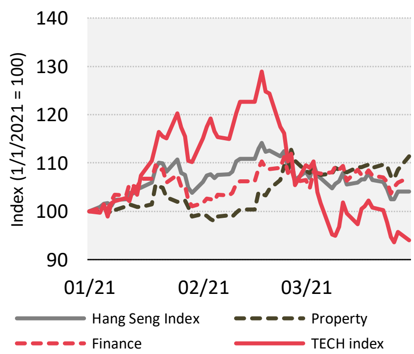
The Hang Seng Index closed at 28,338.3 points on 29th March, 2021, representing a fall of 2.2% from the end of February. In comparison, the Shanghai A-share index fell by 2.1% over the same period.

Stock Market Indices



Source: Bloomberg, data as of 29/3/2021

Stock Market Indices



Source: Bloomberg, data as of 29/3/2021

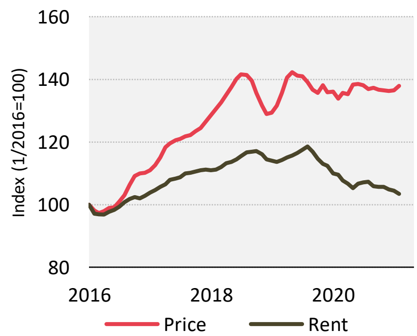
Modest rise in property prices

Residential property prices have been resilient, supported by a supply shortage and low interest rates despite the worst economic performance on record. As of end-February, property prices released by the Rating and Valuation Department were up 1.1% from end-2020. The upswing was mainly led by smaller apartments, which registered a 2.4% rise from end-2020 in prices for flats with 70-100 sqm.

Property transactions were still strong entering 2021, with transaction values rising 75% year-on-year during January and February to HKD 96.6 billion. This increase was led by the secondary market, which saw an annual growth of 90.7%.

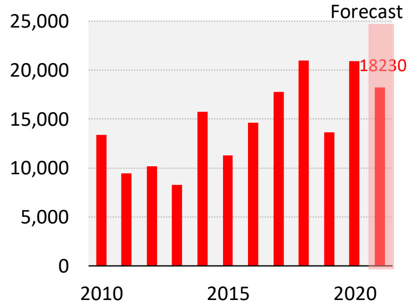
As investors were optimistic about the US economic recovery, the US Treasury 10-year bond yield has once risen to breach the 1.7% threshold in March. The market is worried the large-scale fiscal stimulus could fuel inflationary pressure and prompt the US Federal Reserve (Fed) to end its quantitative easing earlier than expected. This would reduce

Housing Price and Rent Indices



Source: Rating and Valuation Department, data as of 29/3/2021 capital flows into the market. Nonetheless, the Fed had earlier projected that by 2023 the inflation rate would remain at or below the central bank's 2% target, suggesting that it will maintain the ultra-low interest rate policy for a considerable time. Currently, the Hong Kong market is still rich in liquidity, and the three-month HIBOR has been hovering at a low level of about 0.23% to 0.25%. In addition, the HKD prime interest rate did not follow US interest rate movement exactly in its last interest rate hike cycle. Therefore, it is expected that the HKD prime rate will remain at its current level for the next one to two years. Meanwhile, Hong Kong's housing supply is still tight. The Rating and Valuation Department estimated that last year's private housing supply was 20,890 units, while this year's would shrink to 18,230 units.

Hong Kong Residential Unit Completions



Source: Hong Kong Rating and Valuation Department, data as of 29/3/2021

Looking ahead, it is expected that Hong Kong's economy will gradually recover when the epidemic is under control. If local vaccination progresses well, social distancing measures can be lifted gradually and economic activities can normalise. The expectation of an economic recovery will increase end-user demand. However, property developers have seen sales slow last year amid the pandemic and social distancing measures. Apartment sales are expected to speed up this year, increasing housing supply. Meanwhile, the unemployment rate remains above 7%, and there are still many uncertainties facing the economy, including a resurgence of the epidemic, volatile US-China relations, and emigration trends from Hong Kong. These will add to downside risks and make end-users hesitant about purchasing property. Therefore, we expect that residential property prices will only rise moderately in 2021.

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